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No. 06-526

In The Supreme Court of the United States

WACHOVIA BANK, N.A.,
Petitioner,

v.

EASTMAN KODAK COMPANY, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

REPLY BRIEF FOR PETITIONER

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PARTIES TO THE PROCEEDINGS AND RULE 29.6 STATEMENT

Petitioner, Wachovia Bank, N.A., is a national bank and a wholly owned subsidiary of Wachovia Corporation, which is a publicly traded company. Petitioner incorporates herein the Rule 29.6 Statement set forth in its petition dated October 16, 2006 (the "Petition").

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REPLY BRIEF FOR PETITIONER

In attempting to resist review by this Court, Kodak demonstrates why review is needed. The brief in opposition is more noteworthy for what it does not say than for what it does.

1. Kodak nowhere denies the profound effect that its tactical maneuverings had on the bankruptcy case. As explained in the petition, Kodak's failure to assert in the bankruptcy court that it was somehow misled into making the $30 million loan to Wolf—or, to be more precise, Kodak's raising that claim in the N.Y. Adversary Proceeding, followed by Kodak's voluntary dismissal of its own action—had a substantial impact on the conduct of the parties and the bankruptcy court.

Among other things, in reliance on the bankruptcy court's rulings, Wachovia advanced $10 million in new loans to Wolf as a debtor in possession; Wachovia agreed to forgo $25

million of the proceeds of its collateral so that administrative creditors could be paid; Wachovia compromised the amount of its claim and consented to distributions to junior creditors who otherwise would have received nothing; and the bankruptcy court confirmed the Plan that implemented the numerous orders and compromises approved during the bankruptcy case. Kodak simply ignores all of this, insisting that it could pick and choose when and how to participate in the bankruptcy case. At no point does Kodak deny that the entire course of the bankruptcy case would have been different if Kodak had contested the effect of the Subordination Agreement on Kodak's $30 million loan to Wolf and on the treatment of Kodak's claim in the bankruptcy case.

2. Kodak tries to defend the court of appeals' statement that the N.Y. Action and the bankruptcy case do not involve a common nucleus of operative fact. Kodak nowhere denies, however, that all of the facts that it pled in the N.Y. Action could have been pled in the bankruptcy case and that all of those facts indeed *were* pled in the bankruptcy case when Kodak commenced the N.Y. Adversary Proceeding. Kodak not only could have injected, but actually did inject, into the bankruptcy case the identical allegations that it now seeks to pursue in separate litigation. Comparison of Kodak's pleadings in the two matters (Pet. App. 182a-199a) makes this point abundantly clear, and Kodak does not deny it.

Kodak apparently contends, however, that by choosing to terminate the N.Y. Adversary Proceeding, Kodak could control what was or was not included in the "nucleus of operative fact" before the bankruptcy court and thus could dictate the res judicata effect of the bankruptcy case. But that is not the law. Res judicata does not depend on litigants' self-serving tactics, but rather on practical considerations regarding the nature of the controversy adjudicated by the courts. *Sure-Snap Corp. v. State St. Bank & Trust, Co.*, 948 F.2d 869, 873 (2d Cir. 1991) (res judicata encourages reliance on adjudica-

tion by barring "re-litigation not just of those claims which were brought in a prior proceeding, but of 'any other admissible matter' which could have been brought") (quoting *Comr. v. Sunnen*, 333 U.S. 591, 597 (1948)); *Allen v. McCurry*, 449 U.S. 90, 94 (1980). Here, where the triangular relationship among Wolf, Kodak, and Wachovia was at the heart of the matters addressed in the bankruptcy case, Kodak should not be permitted to insist that a part of that controversy must be resolved in separate litigation after the fact.

The attempt to treat the N.Y. Action as distinct from the proceedings in the bankruptcy court rejects the test that claims are measured by the underlying facts, transactions, and occurrences that give rise to the claim, not the legal remedies or theories of relief alleged. The orders entered by the bankruptcy court did not address Kodak's claims against Wachovia for damages or equitable subordination because Kodak determined not to pursue them in the bankruptcy court when the validity, enforceability, and effect of the Subordination Agreement were being determined. But no litigant should be permitted to attempt to manipulate the res judicata effect of court proceedings in this way, particularly where the subsequent action could lead to inconsistent judgments.

Indeed, correctly applying the test, other circuits, including the Second and Third, would preclude the N.Y. Action on res judicata grounds. For example, in *CoreStates Bank, N.A. v. Huls America, Inc.*, 176 F.3d 187 (3d Cir. 1999), the debtor proposed a plan of reorganization that treated creditors in a manner contrary to the terms of a subordination agreement. The senior creditor objected to the plan on grounds that did not include the alleged violation of the subordination agreement. The objection was overruled and the plan confirmed. The senior creditor then commenced a separate action against the junior creditor to recover damages for breaching the subordination agreement. The court held that the subsequent action was precluded by the confirmation order even though

the senior creditor did not previously assert the effect of the subordination agreement as part of its plan objection. The Third Circuit ruled that the senior creditor "could have" raised the subordination agreement as part of the bankruptcy court's consideration of the plan, stating:

> We conclude that there was no reason CoreStates could not have brought its current claim before the bankruptcy judge. . . .
>
> * * *
>
> Although CoreStates submits that the dispute is entirely between itself and Huls—and thus does not impact the debtor at all—we believe it clear that the resolution of this dispute conceivably would have impacted upon the debtor's options in crafting a plan that met with Huls' approval and thereby affected the handling of the bankruptcy estate.
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> * * *
>
> Raising an objection to a reorganization plan can be a claim for claim preclusion purposes. . . .
>
> * * *
>
> The more significant question, then, is whether CoreStates's present cause of action is essentially the same as that which it raised in its objection to the Plan. We think it is apparent that the objection and CoreStates's present claim addressed the same factual issue: who should receive and retain the $600,000 UCT was prepared to pay. Although, as CoreStates contends, its legal claims concerning this money may rest on somewhat different grounds in the two proceedings, the "same cause of action" requirement relates to the factual circumstances underlying the claims, not their legal basis.

176 F.3d at 203-06.

Similarly, *In re Best Products*, 68 F.3d, 26, 28, 31-32 (2d Cir. 1995), involved a plan that enforced a subordination agreement under which the junior creditors received no distribution and the senior creditors compromised numerous aspects of their claims. The junior creditors first objected to the plan on the ground that alleged fraud by the senior creditors required the court to disregard the subordination agreement. After the objection was overruled, the junior creditors claimed that they were not bound by the plan on the grounds that: (a) the bankruptcy court lacked jurisdiction to enforce an intercreditor subordination agreement; and (b) in any event, an intercreditor contract dispute could not be resolved in the context of a contested confirmation hearing, but rather required an adversary proceeding. The Second Circuit rejected these contentions, holding:

> RTC strongly urges that the present controversy merely involves RTC and the Bank Group, and does not concern the Debtor in any way. However, the Subordination Agreement . . . sets forth the relative priority of *Best's* obligations. Moreover, the fact that Best filed briefs and argued in favor of enforcing the Subordination Agreement in both the district court and this court belies the claim that Best had no interest in this controversy. Determination of the priority rights of various creditors to assets of the Debtor was necessary to administer the estate and was not merely a dispute between two creditors.
>
> * * *
>
> In its careful opinion, the bankruptcy court properly made this determination. Both the Settlement and enforcement of the Subordination Agreement were provisions of the Plan, which was confirmed according to proper procedure. RTC's assertion that it was entitled to a full determination of the merits of its claim that the Bank Group's notes never became "due" is therefore meritless.

68 F.3d at 32-33. The only difference between *Best Products* and this case is that Kodak abandoned claims concerning the

Subordination Agreement that it actually raised in the bankruptcy case in the New York bankruptcy court, and that it *could have* raised in the Atlanta bankruptcy court. As held in *Sure-Snap,* however, that difference is immaterial:

> Although Sure-Snap takes the standard set forth in Restatement (Second) of Judgments, § 30, as proof that a reorganization hearing is conclusive only with regard to *non-property* related issues which were *actually* litigated, the well-established rule . . . asserts that "any attempt by the parties or those in privity with them to relitigate any of the matters that were raised *or could have been raised therein* is barred under the doctrine *res judicata.*"

948 F.2d at 873 (quoting *Miller v. Meinhard-Commercial Corp.*, 462 F.2d 358, 360 (5th Cir. 1972)); *see also* Petition p. 24.

3. Kodak maintains that it could not have obtained from the bankruptcy court all of the relief that it has demanded in the N.Y. Action. Kodak's focus is far too narrow. It asks the wrong question and not surprisingly gets the wrong answer. The issue is not whether the bankruptcy court, acting alone, could have granted Kodak all of the compensatory and exemplary relief it seeks. The issue is whether Kodak could have obtained such relief from the bankruptcy court and its supervising district court, acting together. The answer is yes, and Kodak does not deny it.

Kodak's approach to res judicata in bankruptcy—determining the scope of the doctrine by reference to the bankruptcy court's remedial authority rather than by reference to the substance of matters within the bankruptcy court's core or "related to" jurisdiction—has been rejected by the Second, Third, Sixth, Ninth, and Tenth Circuits (Petition pp. 28-29). In *CoreStates*, 176 F.3d at 197-98, for example, the court held "that the restrictions on a bankruptcy judge's judicial power with respect to non-core 'related' claims do not limit the

effect of the doctrine . . . ." The Third Circuit further explained that "a limitation on judicial power is not a limitation on jurisdiction. Section 157(c) only limits a bankruptcy judge's power to grant relief, not jurisdiction over a proceeding requesting such relief." Similarly, in *Sure-Snap*, 948 F.2d at 873, the court dismissed the distinction between core and non-core matters as having "no bearing" on the doctrine of res judicata.[1]

There is no dispute that: (i) the bankruptcy court had jurisdiction to enter the Financing Order, the Sale Order, the Settlement Order, and the Confirmation Order; (ii) the Subordination and Intercreditor Agreements were integral to the bankruptcy court's determinations in each of those orders as to the relative priority and treatment of Wachovia's and Kodak's claims; (iii) the parties to the bankruptcy case relied on the positions taken or not taken during the case and the orders entered by the bankruptcy court; (iv) the administration of the bankruptcy case was directly affected by Kodak's tactical decisions; (v) the bankruptcy court had either core or "related to" jurisdiction to consider all claims, defenses, or other matters that parties to the Subordination Agreement *could* assert in connection with the bankruptcy court's determination of intercreditor priorities;[2] and (vi)

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[1] *In re Piper Aircraft*, 244 F.3d 1289 (11th Cir. 2001), on which Kodak relies (Kodak Brief p.16), is not to the contrary. In *Piper* the court held that a dispute between two creditors that arose post-confirmation by virtue of an alleged breach of an agreement to co-sponsor a plan of reorganization could have no impact on the administration of the bankruptcy estate and that the bankruptcy court lacked jurisdiction to address the breach of contract claims that were neither raised during the confirmation hearing, nor relevant to the outcome of such hearing.

[2] *See In re Best Products*, 68 F.3d at 28, 31-32. Contrary to Kodak's misstatement that "related to" jurisdiction is limited to matters affecting the actual distribution of estate property (Kodak Brief pp. 17-18), the Third Circuit in *Pacor, Inc. v. Higgins*, 743 F.2d 984, 994 (3d Cir. 1984) held that to be related, the action need not necessarily be against the

consistent with Kodak's own allegations in the N.Y. Adversary Proceeding, the bankruptcy court, together with the district court, could have awarded Kodak *all* of the relief sought in the N.Y. Action.

4. Both the Eleventh Circuit and Kodak pay only lip service to the proposition that res judicata precludes the litigation of claims that could have been raised (Kodak Brief p. 14). Kodak points to the Eleventh Circuit's statement to this effect (Pet. App. 10a) as support for Kodak's contention that, notwithstanding the disparities described above, the circuits are uniform in their approach to res judicata in bankruptcy cases. Kodak thus exalts the ability of courts to state the rule over its proper application.

Indeed, Kodak claims (Kodak Brief p.14) that the court of appeals correctly relied on *CoreStates* to support an application of res judicata that bars subsequent intercreditor claims *only if* such claims were *actually* litigated.[3] Not only is such an application in conflict with established precedent from this

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debtor or the debtor's property, as long as the outcome "could alter the debtor's rights, liabilities, options, or freedom of action . . . [and] in any way impacts upon the handling and administration of the bankrupt estate."

[3] Kodak's reference to the Enron bankruptcy (Kodak Brief p. 18) as support for the proposition that it is impractical or impossible to require *all* intercreditor claims to be brought or barred by res judicata proves too much. First, there is no suggestion by Wachovia, or by any federal court of appeals, that all claims, regardless of their nexus to the first action, must be brought or precluded. To the contrary, Wachovia agrees with the basic principle that the two actions must have a logical nexus such that res judicata will apply to preclude a separate action that "would impair or destroy rights or interests" established in the first action. *See, e.g., Sure-Snap.*, 948 F.2d at 874; *CoreStates*, 176 F.3d at 200. Second, *Enron* is a complex case involving numerous settlements and preserved claims. It is improper to refer to the pendency of post-confirmation intercreditor disputes that are not part of any record in these proceedings, particularly without any description of the claims and how they were treated in Enron's plan of reorganization.

Court and other circuits (Petition pp. 21-26), but it is a misreading of *CoreStates*. The Third Circuit limited res judicata to subsequent claims between creditors only where such claims had not accrued as of the commencement of the first action. *See CoreStates*, 176 F.3d at 204. In contrast, where, as in the N.Y. Action, all of the facts, transactions, and occurrences on which the subsequent action is based occurred before the commencement of the bankruptcy case, the circuits have uniformly held that the claim could have been considered and res judicata will apply. *Compare In re Piper Aircraft*, 244 F.3d at 1289 (cause of action for breach of contract accrued only after the bankruptcy court confirmed a plan that was not proposed by the plaintiff and defendant and thus could not have been brought during the confirmation hearing), with *CoreStates*, 176 F.3d at 204-05 (action referring to enforcement of a pre-petition subordination agreement was based on pre-petition acts that could have been asserted during bankruptcy case).

5. Finally, although Wachovia is not seeking review of factual issues, the Court's consideration of the petition should be informed by an accurate statement of the facts. Wachovia therefore highlights the following factual points, which were either misstated or ignored by Kodak:

- The Intercreditor Agreement required each party to use best efforts to notify the other of certain "actions" taken, not of events or information received (*compare* Kodak Brief p. 2).
- The $30 million was used to reduce Wolf's revolving line of credit; that amount could have been reborrowed under the credit agreement (*compare* Petition p. 4; Kodak Brief p. 3).
- Kodak elected to fund the $30 million loan before receiving Wachovia's consent, which Kodak's own loan documents made a condition precedent to Wolf's receipt of the $30 million (*compare* Petition p. 3; Kodak Brief p. 4).

- Wachovia's March 2, 2000 limited consent to Wolf's breaches of financial covenants was *not* conditioned on Kodak providing any loan to Wolf or on Wachovia's receipt of any proceeds of such a loan (*compare* Kodak Brief p.3).
- Although not a signatory to every stipulation of settlement, Kodak was bound by all of the orders of the bankruptcy court, including those approving such settlements (*compare* Petition pp. 5-13; Kodak Brief p. 6).
- The N.Y. Action was first commenced as the N.Y. Adversary Proceeding, wherein Kodak alleged that the New York bankruptcy court had core jurisdiction to equitably subordinate Wachovia's claims to Kodak's and to award Kodak damages for breach of contract and fraud (*compare* Petition pp. 8-9; Kodak Brief p. 6).
- The N.Y. Action was commenced contemporaneously with the filing of Wolf's Plan in the bankruptcy court and was fundamentally inconsistent with the treatment of claims set forth in the Plan (*compare* Petition pp. 8-13; Kodak Brief p. 7).

CONCLUSION

For all of the foregoing reasons, in addition to those set forth in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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